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IN THE

Supreme Court of the United States

OCTOBER TERM 1935

C. L. ASHTON ET AL. ..... *Petitioners,*

v. No. 859

CAMERON COUNTY WATER IMPROVEMENT DISTRICT NUMBER ONE

MOTION FOR LEAVE TO FILE BRIEF AS *AMICUS CURIAE* AND BRIEF AS *AMICUS CURIAE*

CHAS. D. FRIERSON,

Counsel for Drainage District Number Seven, of Poinsett County, Arkansas, and other districts as Amicus Curiae.

DEMOCRAT P. & L. CO., LITTLE ROCK

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MOTION FOR LEAVE TO FILE BRIEF AS *AMICUS CURIAE*

May it Please the Court:

The undersigned, as counsel for Drainage District Number Seven, of Poinsett County, Arkansas, and several other drainage and levee districts in Arkansas, respectfully moves this Honorable Court for leave to file the accompanying brief in this cause as *amicus curiae.*

.....

CHAS. D. FRIERSON,
Counsel for Drainage District Number Seven, of Poinsett County, Arkansas, and other districts as Amicus Curiae.

IN THE SUPREME COURT OF THE UNITED STATES

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CAMERON COUNTY WATER IMPROVEMENT DISTRICT NUMBER ONE

BRIEF OF CHAS. D. FRIERSON AS *AMICUS CURIAE*

I.

PRELIMINARY STATEMENT

The interest of the undersigned in the litigation rests upon the fact that he is counsel for several drainage and levee districts in Arkansas which are being refinanced with the consent of more than 90% of bondholders in each case, and in order to make the compromise effective, it may be necessary for the districts to follow Section 80 of the Bankruptcy Act, being the Municipal Debt Readjustment Act.

Drainage District No. 7, Poinsett County, Arkansas, one of the largest drainage districts in the South, is now in bankruptcy under this Act; its petition was filed on July 12, 1934, and 98% of creditors have accepted the plan to refinance at 25.879c on the dollar of principal. By the plan, an outstanding issue of $5,600,000 of bonds will be refinanced by an issue of

about $1,650,000; the interest rate and the annual tax rate will be reduced.

Default of the district resulted from excessive floods, bank failures and the general financial depression, so that without scaling down the debt the lands of the district could never pay the bonds together with the long accumulated interest. The holders of only $25,000 of bonds are actively contesting the plan and the remaining bonds of the $112,000 or so still outstanding simply have not expressed either approval or rejection, considerable blocks of such bonds being held in trust in such manner that they cannot be delivered until the final decree in the Bankruptcy Court. The evidence has been taken and the Special Master's report upholding the Readjustment Plan has just been filed and the whole case should reach a final decree within thirty days from this date. Hence the decision of this Honorable Court in the present case will determine action upon the refinancing plan of said district and this case is of extreme importance to said district.

In addition to Drainage District No. 7, the undersigned represents also the following drainage and levee districts in Arkansas, all of which may be affected to a considerable extent by the determination of the present suit, and in each case more than 90 per cent of the bondholders are in favor of the plan, these districts being:

First Slough Drainage District of Greene and Craighead Counties, Arkansas, former bond issue, $32,-

000 being refunded at 50 cents on the dollar of the principal.

Cane Island Drainage District No. 26, of Craighead County, Arkansas, the former bond issue being about $120,000; the plan accepted by all, except $4,000 in bonds, being 60 cents on the dollar of the principal.

Little Bay and Whiteman's Creek Drainage District No. 20 of Craighead County, Arkansas, former bond issue, $102,500 being refunded at 60 cents on the dollar of the principal, and only $4,000 or $5,000 of the bonds not having consented.

Bay and St. Francis Drainage District No. 29, of Craighead County, Arkansas, an outstanding bond issue of $457,000 to be refinanced at about 65 cents on the dollar, all except a very few thousand dollars of the bonds agreeing thereto.

Village Creek and White River Levee District, of Jackson County, Arkansas, an outstanding bond issue of $55,000, being refinanced at about 60 cents on the dollar of the principal debt, all bondholders agreeing.

Long Prairie Levee District of Lafayette County, Arkansas, with a bond issue in the neighborhood of $150,000, the plan of refinancing being at 60 cents on the dollar of the principal and a large majority of the bondholders favoring it.

Experience proves that in the refinancing of such districts a few bondholders or creditors refuse to join the plan, hoping thereby to obtain a larger dividend or settlement rate than those who co-operate. This

experience, historically, is what caused the passage of Section 80 added to the Bankruptcy Act permitting municipal corporations and improvement districts, with the consent of a fixed percentage of their bondholders, to force through a composition upon the minority creditors. In practically every large district a few bonds do not co-operate, either because they are tied up in trust funds and cannot be voted for the debt plan, or else because their owners desire a larger percentage than satisfies the majority of the creditors.

The writer's contention is that Section 80 is a valid Bankruptcy Act and does not violate the Constitution.

We have not had an opportunity to inspect the record further than the opinions of the District Court and of the Circuit Court of Appeals in this cause. We shall not attempt to discuss any of the particular details of this individual case, but simply to express briefly our views that the Act is Constitutional and, of course, our conviction that it is highly essential and necessary for the welfare of those districts within our knowledge.

Our understanding is that the petitioners base the argument of unconstitutionality upon two propositions, the first being that Congress does not possess authority to pass a Bankruptcy law for relief of an arm of the State, and, second, upon the point that the Act violates the Tenth Amendment to the Federal Constitution in that it invades the reserved powers or the sovereign rights of the State. Further the contention may be made that it is not a valid bankruptcy act.

II.

ARGUMENT

Section 80, the Municipal Debt Adjustment Statute, amending the Bankruptcy Law, does not invade State sovereignty and it is valid for the following reasons:

POINT A.

AN IMPROVEMENT DISTRICT IN ARKANSAS AND OTHER STATES IS NOT AN ARM OF THE STATE FOR ANY GOVERNMENTAL PURPOSE BUT IS AN AGENCY OF THE TAXPAYERS.

In Arkansas and some, if not all, other States, a drainage, levee or other improvement district is definitely *not* an arm of the State for any general governmental purpose. It is only a public quasi-corporation given for very limited purposes the powers of taxation by special assessment and of eminent domain. Its governing board is an agency for its taxpayers. The statute gives it the power to sue and be sued just like private corporations (except for a partial immunity from tort actions). It may compromise and adjust claims as an incident to its liability to suit. Hence we contend that Section 80 does not concern States sovereignty.

> "Hence it will be seen that, if the proposed acts of Drainage District No. 7 of Poinsett County were to be committed by a railroad corpora-

tion, by a private corporation, or by a private person, the venue of the action would be in Cross County where the land is situated and service would be had upon the defendant in Poinsett County, where the act sought to be enjoined was alleged to be committed. But it is insisted that this rule does not apply to a drainage district. We do not agree with counsel in this contention. It is true that drainage districts, levee districts, and road improvement districts are created by statute, and have only such powers as are expressly or impliedly conferred upon them. They are quasi-public corporations with power to sue and be sued with reference to the matters conferred upon them. *Altheimer* v. *Board of Directors of Plum Bayou Levee District*, 79 Ark. 229, 95 S. W. 140; *Board of Directors of St. Francis Levee District* v. *Fleming*, 93 Ark. 490, 125 S. W. 132; and *Board of Levee Inspectors of Chicot County* v. *Southwestern Land & Timber Company*, 112 Ark. 467, 166 S. W. 589. According to these and numerous other decisions of this court, local improvement districts and their commissioners are governmental agencies created as quasi-public corporations deriving their powers directly from the Legislature and exercising them as the agent of the property-owners in the district whose interests are affected by the duties they perform. They exercise no governmental powers except those expressly or impliedly granted by the Legislature. They are not political or civil divisions of the State like counties and municipal corporations created to aid in the general administration of the government. They are not created for political purposes or for the administration of civil government. Hence no public policy would be violated by applying the same rules for the service of

process upon them as are prescribed for private corporations and quasi-public corporations, such as railroads, etc."

Drainage District 7 v. *Hutchins*, 184 Ark. 520, (42 S. W. 2nd 996).

The action of the Board of a drainage district binds the district in like manner as a board of directors binds a private corporation.

Caldwell v. *Guardian Trust Co.*, (C. C. A. 8), 26 F. 2d 218.

This court has discussed the nature of such districts in

Hagar v. *Reclamation District*, 111 U. S. 701.

Houck v. *Little River District*, 239 U. S. 254.

There are innumerable instances in this court where counties, school, drainage, levee and irrigation districts, and other public quasi-corporations created by States have been sued and hence it is certain that they do not partake of the State's immunity to suit. A few instances are:

The County of Lincoln v. *Luning*, 133 U. S. 529.

County of Mercer v. *Hackett*, 1 Wall. 83.

Com'rs Knox County v. *Aspinwall*, 21 How. 539.

Hopkins v. *Clemson College*, 221 U. S. 636.

Litchfield v. *County of Webster*, 101 U. S. 773.

Guardian Sav. & Trust Co. v. *Road Imp. Dist. 7*, 267 U. S. 1.

Mercantile Trust v. *Wilmot Road Dist.*, 275 U. S. 117.

Exchange Trust v. *Drainage District 7*, 278 U. S. 427.

POINT B.

DRAINAGE AND OTHER IMPROVEMENT DISTRICTS HAVE ALWAYS BEEN SUBJECT TO SUIT IN THE FEDERAL COURTS AND EVEN TO RECEIVERSHIP AND MANDAMUS.

Since such suits are not invasions of sovereignty, certainly Section 80 of the Bankruptcy Act permitting a district to go voluntarily into court for a friendly composition of debts does not appear to be any invasion of sovereignty.

This point is a corollary of Point A, and the authorities to that point apply to this. The very idea of an "invasion" of sovereignty implies some forcible intrusion or action from the outside. It seems to us it cannot apply to a permissive statute under which a district must voluntarily come into court, if it comes into court at all, for a friendly settlement with its creditors. Particularly does this seem true when there is required not only voluntary action by the district, but also voluntary consent of a large percentage of its creditors, before jurisdiction under Section 80 can attach.

Sec. 80 of Bankruptcy Act, Ch. 345, 48 Stat. 798, USCA Tit. 11 Sec. 303.

That an act merely permissive in its nature does not invade State sovereignty seems to be held in

Massachusetts v. *Mellon*, 262 U. S. 447:

"What, then is the nature of the right of the State here asserted, and how is it affected by this statute? Reduced to its simplest terms, it is alleged that the statute constitutes an attempt to legislate outside the powers granted to Congress by the Constitution and within the field of local powers exclusively reserved to the States. Nothing is added to the force or effect of this assertion by the further incidental allegations that the ulterior purpose of Congress thereby was to induce the States to yield a portion of their sovereign rights; that the burden of the appropriations falls unequally upon the several States; and that there is imposed upon the States an illegal and unconstitutional option either to yield to the Federal Government a part of their reserved rights, or lose their share of the moneys appropriated. But what burden is imposed upon the States, unequally or otherwise? Certainly there is none, unless it be the burden of taxation, and that falls upon their inhabitants, who are within the taxing power of Congress as well as that of the States where they reside. Nor does the statute require the States to do or to yield anything. If Congress enacted it with the ulterior purpose of tempting them to yield, that purpose may be effectively frustrated by the simple expedient of not yielding.

"In the last analysis, the complaint of the plaintiff State is brought to the naked contention that Congress has usurped the reserved powers of the several States by the mere enactment of the statute, though nothing has been done and nothing

> is to be done without their consent; and it is plain that that question as it is thus presented is political, and not judicial, in character, and therefore is not a matter which admits of the exercise of the judicial power" (pp. 482, 483).

The language of the act very specifically provides only for voluntary action by the district and no district can be forced into the Bankruptcy Court against its will. The purpose of the act is to permit such a district and other municipal corporations the privilege of making a friendly compromise of debts with a majority of its creditors and to render that composition effectual by giving it the status of a bankruptcy or insolvency proceeding in the Federal Court. This is a great privilege and is not an invasion.

POINT C.

SECTION 80 EXPRESSLY PROHIBITS INTERFERENCE WITH GOVERNMENTAL FUNCTIONS IN THE FOLLOWING LANGUAGE:

> "Nothing contained in this chapter shall be construed to limit or impair the power of any State to control, by legislation or otherwise, any political subdivisions thereof in the exercise of its political or governmental powers, including expenditures therefor."
>
> Sec. 80, Bankruptcy Act, Ch. 345, 48 Stat. 798; USCA 11, Sec. 303 (k).

The foregoing language seems a very careful attempt to preserve intact State sovereignty including all governmental and political powers and even State con-

trol over expenditures. In this connection the point seems to have been raised in the lower court that before a drainage district can take advantage of the Act the State must first pass an act permitting such a district to avail itself of the Bankruptcy Act. This argument is well answered in the opinion of the Circuit Court of Appeals in the present cause. That court points out that the act itself is limited in its operation to a two-year period and that to require the States first to pass permissive acts would render Section 80 useless in many instances because the State Legislatures would not all meet within the effective period of the act. The act itself is perfectly clear that it is available to a district without separate State legislation; but it is provided that if there be such legislation, then it must be complied with by the district. In the State of Arkansas the next session of the General Assembly after the passage of this act of Congress was early in 1935. Had Drainage District No. 7 delayed hoping for a permissive act to be passed, it would have been financially ruined, because creditors were then pressing it vigorously and many suits were pending. Furthermore, the State of Arkansas did not pass a permissive act even at the session of 1935 nor ever, but apparently has taken the position that the act of Congress in itself filled the entire field.

Hence, in all the districts represented by the undersigned, there has been a total absence of State legislation on the subject; and unless these districts can voluntarily avail themselves of the Congressional stat-

ute they are financially ruined and permanently. For instance the bonds of one of these districts at about the time this act was passed, were selling in the open market at 5 cents on the dollar, and by the Debt Readjustment Plan the owners received nearly 26 cents on the dollar.

POINT D.

NO STATE INSOLVENCY LAW COULD BE EFFECTIVE, BECAUSE NO STATE COULD PASS A LAW IMPAIRING THE OBLIGATION OF A CONTRACT, NOR CAN A STATE PASS ANY INSOLVENCY LAW THAT WOULD FILL THE FIELD OF CONGRESSIONAL BANKRUPTCY LAWS.

International Shoe Co. v. *Pincus*, 278 U. S. 261, and cases cited therein.

As to the broader scope of the Federal Bankruptcy Acts see

Continental Illinois Nat. Bank v. *C. R. I. & P. Ry.*, 294 U. S. 648, and cases cited therein.

POINT E.

UNDOUBTEDLY SECTION 80 IS AN ACT ON THE SUBJECT OF BANKRUPTCY.

This court has so recently passed upon and reviewed the authorities upon this question that certainly no elaboration is required in argument. The power of Congress extends to all forms of legislation regarding

insolvency; and composition of this identical type has been upheld as to private corporations.

Canada Southern R. R. v. *Gebhard*, 109 U. S. 527.

Continental Ill. Nat. Bank v. *C. R. I. & P.*, 294, U. S. 647, *supra.*

In re *Imperial Irrigation Dist.*, (D. C.), 10 F. Supp. 832.

Hanover Nat. Bank v. *Moyses*, 186 U. S. 181.

Section 80 is very closely akin to the Corporate Debf Reorganization Act which has been consistently upheld in the Federal lower courts and finally in this Honorable Court in the case above cited. Minor differences exist on account of the different types of insolvents provided for in the respective acts, but their general substance is the same. In each case it is provided that the insolvent may come into court in conjunction with a specified number or percentage of its creditors and may compromise its debts and readjust liens and equities, even impairing the obligation of contracts.

The proviso, of course, is that such a composition may be provided for only by the consent of the specified majority of creditors of each particular class. However, with such consent, existing liens and contractual rights may be changed.

Of course a later State law on insolvency cannot change nor impair the obligation of any contract, but Congress has this power.

CONCLUSION

In each district which avails itself of Section 80, insolvency must exist to the extent at least provided by the terms of the act, and no readjustment plan can be upheld until it pleases the required majority of creditors of each class, nor unless found by the court to be fair and equitable. In substance it is a composition act. No district can be dragged into court under Section 80, although it can be dragged into court by suits for receivership, mandamus and for other remedies much more drastic than a composition.

(Parenthetically, the right to receivership in Arkansas has been abolished by a recent act, but it was expressly upheld while in force and even today hundreds of districts are operating in Federal receiverships which were in force prior to the act prohibiting receivers.)

No one complains of the jurisdiction of the Federal Courts in the suits of bondholders to grant judgment, mandamus, injunction or other remedy to compel payment. If this well recognized jurisdiction does not constitute an invasion of State sovereignty, nor intrude upon the reserved powers of the State, then it seems manifest to us that the mild and healing remedy of permitting an improvement district or municipal corporation to come into court arm in arm with the majority of its creditors and make a composition according to its ability to pay certainly does not con-

stitute an intrusion upon State sovereignty. It is not a violation of any State's right because States have no rights to pass insolvency or bankruptcy acts, but that right is expressly given to the Federal Government.

A bankruptcy or insolvency statute always impairs contracts; but no State Legislature can pass a law permitting impairment of contract obligations. Hence if the Federal Government cannot permit such compositions through its Bankruptcy court, then the situation is one impossible to meet and bondholders in many instances practically will be unable to collect; the particular district may be absolutely unable to pay, and its lands may not be of sufficient value to justify the bondholders in accepting those lands as payment. Many of these districts have levied taxes until there is a grave question as to whether or not they have exceeded the assessed benefits, and hence the margin of security to the bondholders is extremely narrow. In such districts the bondholders are even more interested in obtaining a composition than are the taxpayers of the district.

In improvement districts the benefits are assessed upon an estimate in advance of the result of the improvements. Excessive floods and financial depression have shown that such estimates were excessively high. Lands which were expected to be put in cultivation after construction of drainage and levee works are still wild and their market value has dropped to an insignificant sum. Thus the burden upon cultivated lands

has increased in many instances so that even those lands cannot carry the increased rate necessary to meet existing bonds and interest.

The act should not be looked upon merely as conferring a one-sided benefit upon taxpayers and districts at the expense of bondholders; but it is equally beneficial to the bondholders in that they can obtain a fair cash settlement and may go into court and prevent bondholders who refuse to co-operate from attempting to obtain a preference by their refusal to join in the composition.

If this statute constitutes an invasion of State sovereignty or of the reserved rights of the State, then certainly those invaded welcome the invasion. This act will be the salvation of taxing districts burdened beyond their capacity and at the same time will be the salvation of bondholders who hold obligations of the district beyond the capacity of the district to pay.

It is an act evidencing broad statesmanship and we respectfully urge that it is a valid and constitutional act, and that the decision of the Circuit Court of Appeals upholding it should be affirmed.

Respectfully submitted,

.....

Chas. D. Frierson, for Drainage District No. 7 of Poinsett County, Arkansas, and other districts, as *Amicus Curiae*.